Attachment 4

Getting up to speed with IFRS

As U.S. companies accelerate toward International Financial Reporting Standards conversion, internal auditors should consider how to prepare for the transition and the role their department might play.

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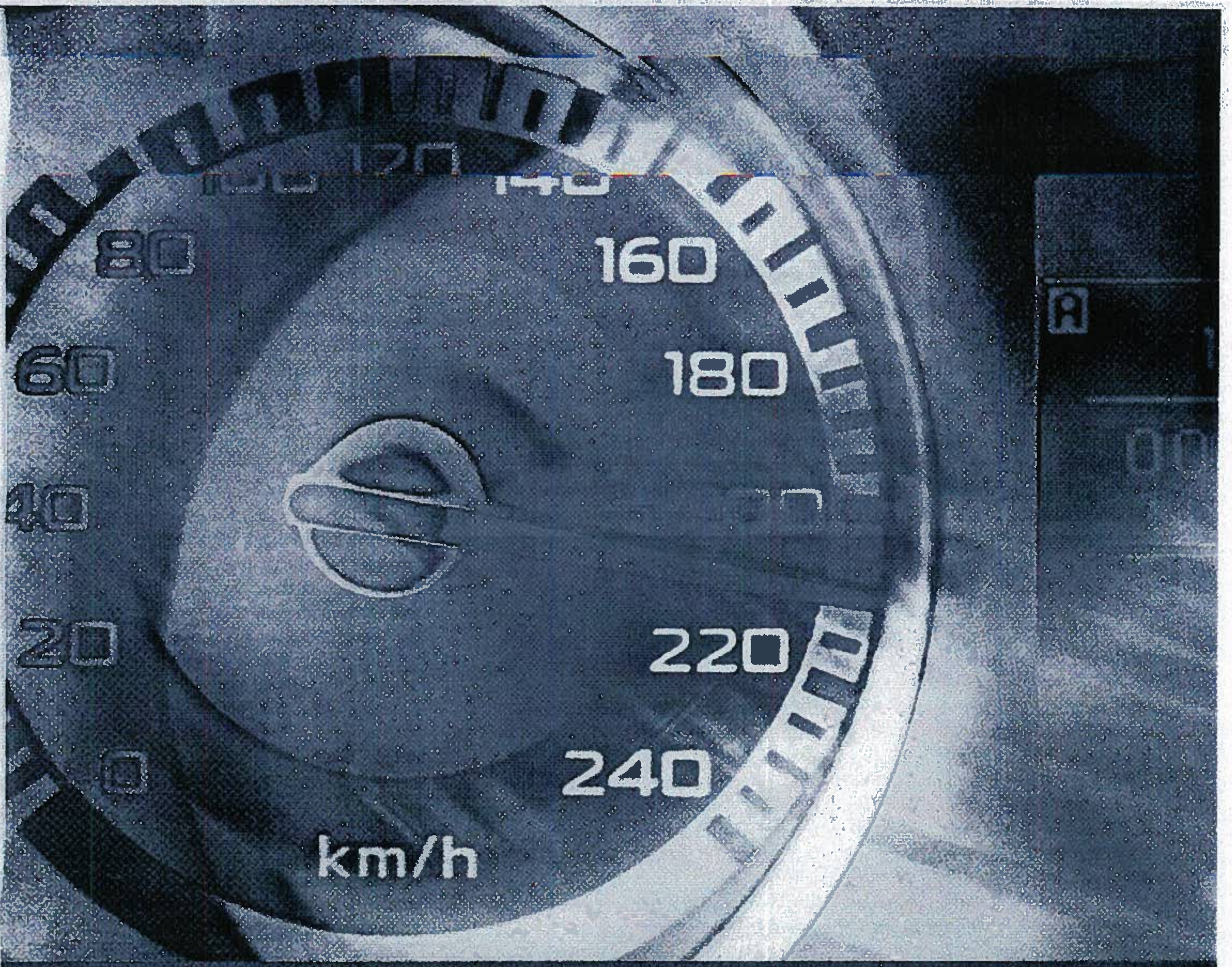
IN A SPEECH HE GAVE TO AN AUDIENCE OF SENIOR FINANCIAL executives this June, John White, director of the Corporate Finance Division at the U.S. Securities and Exchange Commission (SEC), said it was time to face an inconvenient truth: Companies around the world are rapidly migrating to a single set of accounting standards, but they are not U.S. Generally Accepted Accounting Principles (GAAP). Why inconvenient? For years, the idea of a single set of global accounting standards



seemed like an unlikely fantasy, White said. And if accounting rules around the world ever were harmonized, the secret hope was that everyone would adopt U.S. GAAP.

Well, the fantasy has become a reality, but not in the way imagined. Companies around the world have adopted one set of rules, but they are those produced by the London-based International Accounting Standards Board (IASB). More than 100 countries allow or require their companies to use the IASB's International Financial Reporting Standards (IFRS). Others, including Canada and India, are in the process of transition (see "Global Adoption" on this page).

The United States is the only significant player left on the sidelines. But the changeover for U.S. companies could soon be on its way. It's not yet clear what will happen or when, but accounting experts — and internal auditors who have been through an IFRS transition already — say companies should start making plans now.

ON THE HORIZON

Last November the SEC took an historic step in favor of IFRS when it abolished its rule that foreign private issuers had to reconcile their IFRS statements to U.S. GAAP. Now the SEC has published a proposed road map that, if approved, would give the largest U.S. companies the option of moving to IFRS in 2010. Other firms would then be required to use the international standards in three waves. Remaining large firms would switch in 2014, medium ones in 2015, and small ones in 2016. However, the draft road map — which the SEC will vote on after a consultation period that ends in November — allows the SEC to scrap the entire project in 2011 if certain criteria have not been met. These include greater convergence between IFRS and U.S. GAAP, more independence and accountability at the IASB, and better training for U.S. accountants. When the road map was published, SEC Commissioner Elisse Walter stressed that a move to IFRS was by no means definite. "We have to keep in mind that no one knows for certain what the future will hold," Walter said. "I strongly believe that we have to prepare for the alternative that the commission will determine not to adopt, or permit the use of, IFRS for U.S. issuers."

One thing that's clear is that U.S. companies have so far not done much to prepare for this momentous change. White noted in his speech that, for many in U.S. business, the idea of abandoning U.S. GAAP for IFRS was "an idea that seemed so far-fetched it was not worth learning about." That's confirmed by a recent survey from the American Institute of Certified Public Accountants, which found that only 17 percent of its members were actively preparing for a move to IFRS.

But then why should they? "To move forward with such a significant project, companies need a clear understanding of the end requirements before they can develop the necessary systems and procedures and address the critical business issues," says Christine DiFabio, vice president of technical activities at Financial Executives International, a New Jersey based business association for senior financial executives. "It is difficult for most companies to justify major resource allocations or preparatory actions until the key policy makers and regulators provide some firm direction and a timetable to drive the process. Smaller organizations in particular do not have the resources to spend time and money preparing until they feel confident as to the SEC's next steps and requirements."

Global Adoption

More than 100 countries around the world now allow or require their listed companies to produce accounts under IFRS. All of the European Union's (EU's) 27 member states use the standards. Canada and India will be using them by 2011, as will South Korea, with early adoption encouraged from 2009. Japan has pledged to eliminate all major differences between its national standards and all existing IFRS by 2011.

The question of how countries have actually gone about adopting IFRS is a more complicated one, says Patricia O'Malley, director of Implementation Activities at the IASB. A single, universal model for adopting IFRS does not exist, she explains. "Countries have each gone at it in a way that makes sense given their existing framework."

In Europe, for example, the quickest way to implement IFRS was to formally require their use under an EU regulation. But because such a regulation has legal force, the process for formally adopting any new standards is very slow (for example, they have to be translated into every European language first). Sometimes, the EU hasn't been able to adopt a new standard before its application date. This process can cause serious problems for companies with U.S. listings, O'Malley says, because the SEC only exempts foreign companies from producing a U.S. GAAP reconciliation if they use IFRS as issued by the IASB, not IFRS as endorsed for use in the EU.

When it adopted IFRS, the Australian Accounting Standards Board (AASB) decided at first to keep some existing national implementation guidance for issues not covered by IFRS, as long as that guidance didn't conflict with IFRS. This decision caused confusion, as investors weren't sure whether companies were complying with true IFRS, or with an Australian-flavored version. The AASB decided to change tack and delete its national guidance. It now adopts IFRS word-for-word from the IASB's standards.

In Canada, the law requires companies to prepare financial statements in accordance with the standards issued by the Canadian Accounting Standards Board (CASB). "You would think this would mean the CASB could simply issue a standard that said 'follow IFRS,'" O'Malley says, "but apparently that's not good enough." The CASB has to follow its own due process for issuing a standard to include an IFRS in its standards, although like Australia it intends to do so word for word.